

Message Text

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SUBJECT:OVERDUE COTTON CONTRACTS

FROM ASSISTANT SECRETARY HABIB FOR AMBASSADOR

1. I WANT TO CALL TO YOUR PERSONAL ATTENTION THE POLITICAL
AND COMMERCIAL CONSEQUENCES WHICH MAY ARISE FROM THE COTTON
CONTRACT DIFFICULTIES DISCUSSED REFTEL. WHILE I HAVE NO
DOUBT THAT YOU ARE FULLY CONVERSANT WITH THE DETAILS
PERTAINING TO YOUR RESPECTIVE COUNTRIES, I AM PERSONALLY
CONCERNED THAT YOU BE AWARE OF THE OVERALL MAGNITUDE AND
SCOPE OF THE PROBLEM IN EAST ASIA, AND THE POLITICAL CON-
SEQUENCES WHICH WOULD LIKELY FOLLOW MASS DEFAULTING ON

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COTTON CONTRACTS.

2. THE BULK OF RAW COTTON SHIPMENTS OCCUR BETWEEN OCTOBER AND APRIL. DECEMBER, JANUARY AND FEBRUARY ARE THE PEAK MONTHS. THE COTTON SHIPPERS ESTIMATE THAT AS MUCH AS 90 PERCENT OF THE COTTON CONTRACTED FOR SHIPMENT THROUGH NOVEMBER HAS NOT BEEN EXPORTED. IN SOME CASES, LETTERS OF CREDIT HAVE NOT BEEN OPENED AND IN OTHERS THE MILLS HAVE REQUESTED A POSTPONEMENT OF SHIPPING DATES.

3. THE FOLLOWING FIGURES, PROVIDED BY U.S. COTTON SHIPPERS, SHOULD SERVE TO INDICATE THE ROUGH MAGNITUDE OF PROBLEM.

A. NUMBER OF BALES PAST DUE FOR SHIPMENT PRIOR TO NOVEMBER 1
 B. NUMBER OF BALES FOR NOVEMBER SHIPMENT FOR WHICH LETTERS OF CREDIT HAVE NOT BEEN OPENED
 C. TOTAL A AND B
 D. TOTAL NUMBER OF BALES UNDER OUTSTANDING EXPORT CONTRACTS

COUNTRY	A	B	C	D
KOREA	78,202	0,761	208,963	828,263
TAIWAN	33,387	36,675	70,062	290,488
PHILIPPINES	43,836	15,233	59,069	110,102
THAILAND	5,550	27,183	32,733	143,100

4. AS THE COTTON SHIPPING SEASON APPROACHES THE PEAK MONTHS OF DECEMBER, JANUARY AND FEBRUARY, WE BELIEVE THERE WILL BE A TENDENCY FOR MILLS ALL OVER EAST ASIA TO DEFER SHIPPING DATES IN THE HOPE THAT CONTRACTS WILL BE RE-NEGOTIATED AT LOWER PRICES. IF LARGE SCALE DEFAULTING OCCURS IN ANY ONE COUNTRY, MILLS IN OTHER COUNTRIES ARE LIKELY TO FOLLOW SUIT. AT PRESENT, THE NUMBER OF BALES OVERDUE FOR SHIPPING IS GROWING AND THE PROBLEM IS SPREADING FROM THE ROC AND THAILAND TO KOREA AND THE PHILIPPINES. SO FAR, NO CONTRACT PROBLEMS HAVE BEEN EXPERIENCED IN HONG KONG AND JAPAN.

5. MASSIVE CONTRACT DEFAULTING WILL AFFECT NOT ONLY
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COTTON SHIPPERS BUT COTTON FARMERS AS WELL. IF DEFAULTING OCCURS, SMALL SHIPPERS WILL NOT BE ABLE TO MEET THEIR FORWARD CONTRACTS TO THE FARMERS. SINCE MANY EAST ASIAN MILLS HAVE OVERBOUGHT AND SOME SMALL MILLS WILL GO OUT OF BUSINESS IN ANY CASE, THE CUMULATIVE EFFECT ON THE COTTON MARKET AND THE INCOME OF AMERICAN COTTON FARMER WILL BE SEVERE. TO PUT THIS IN CONTEXT, DURING THE PAST

TWO SEASONS COTTON PRICES HAVE RISEN AFTER CONTRACTS WERE SIGNED. LAST YEAR PRICE INCREASES WERE VERY SUBSTANTIAL AND MANY OVERSEAS MILLS MADE WINDFALL PROFITS ON MERCHANDISERS AT PRICES WELL BELOW THOSE PREVAILING IN THE WORLD MARKET AT THE TIME OF DELIVERY.

6. CONSIDERABLE POLITICAL PRESSURE HAS ALREADY BEEN BROUGHT TO BEAR BY CONGRESSMEN REPRESENTING THE COTTON PRODUCING STATES: I.E. SENATORS TALMADGE, TOWER, SPARKMAN

AND STENNIS. I HAVE ABSOLUTELY NO DOUBT THAT CONGRESSIONAL PRESSURE WILL INCREASE CONSIDERABLY IF PROGRESS IS NOT MADE IN SOLVING THIS PROBLEM. THIS IS NEITHER IN OUR INTEREST NOR THAT OF YOUR HOST GOVERNMENT.

7. THE SCOPE AND SERIOUSNESS OF THE PROBLEM IS SUCH THAT I ASK THAT YOU PERSONALLY RAISE THIS ISSUE WITH APPROPRIATE OFFICIALS IN YOUR HOST GOVERNMENTS AS SOON AS POSSIBLE. I WOULD WELCOME YOUR ASSESSMENT OF THE POTENTIAL SIZE OF THE PROBLEM IN YOUR RESPECTIVE COUNTRIES AS WELL AS ANY SPECIFIC MEASURES WHICH WE MIGHT TAKE TO ENSURE THAT MASS DEFAULTING DOES NOT OCCUR.

8. IN YOUR DISCUSSIONS WITH THE HOST GOVERNMENT YOU MAY WISH TO NOTE THE FOLLOWING POINTS: FIRST, IN THE PAST TWO CROP YEARS EAST ASIAN MILLS HAVE PROFITED HANDSOMELY BECAUSE UNITED STATES MERCHANDISERS HAVE HONORED THEIR CONTRACTS AT PRICES WELL BELOW WORLD MARKET PRICES AT TIME OF DELIVERY. SECOND, DUE TO THE SLACK TEXTILE MARKET, MANY MILLS HAVE LOW LIQUIDITY POSITIONS RESULTING FROM HIGH INVENTORIES OF FINISHED GOODS. THESE INVENTORIES MIGHT BE STOCKPILED BY THE GOVERNMENT OR ACCEPTED AS COLLATERAL BY THE CENTRAL BANK. THIRD, CREDIT TERMS OR

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COLLATERAL REQUIREMENTS, IN GENERAL, MIGHT BE EASED FOR THE TEXTILE MILLS BY THE MONETARY AUTHORITIES. FOURTH, TEMPORARY TAX RELIEF OR OTHER FISCAL MEASURES COULD BE UNDERTAKEN TO EASE PRESSURES ON THE INDUSTRY. FINALLY, WE BELIEVE IT WOULD BE HELPFUL IF THE HOST GOVERNMENT EXPRESSED TO THE LEADING MILLS AND INDUSTRIALISTS ITS STRONG SUPPORT FOR THE SANCTITY OF CONTRACTS. ALTHOUGH WE REALIZE THE INDUSTRY IS IN A SEVERE RECESSION, THESE CONTRACTS WERE MADE IN GOOD FAITH WITH BOTH PARTIES ACCEPTING BUSINESS RISKS.

9. FYI WE MADE STRONG REPRESENTATIONS ON THIS MATTER TO ROC MINISTER OF ECON AFFAIRS DURING HIS VISIT IN WASHINGTON AND HE PROMISED HE WILL LOOK INTO IT AND TAKE REMEDIAL ACTION. SEPTTEL WILL FOLLOW END FYI. INGERSOLL

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